

1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2
3 COMMISSIONERS

4 MARC SPITZER, Chairman
5 WILLIAM A. MUNDELL
6 JEFF HATCH-MILLER
 MIKE GLEASON
 KRISTIN K. MAYES

In the matter of)	
INTERSECURITIES, INC.)	DOCKET NO. S-03482A-03-0000
570 Carillon Parkway)	
St. Petersburg, Fl 33716-1202)	DECISION NO. <u>67353</u>
CRD# 16164)	
GREGORY RUSSELL BROWN and)	ORDER AND CONSENT TO SAME BY:
KAREN BROWN, husband and wife)	RESPONDENT INTERSECURITIES, INC.
16417 South 15 th Drive)	
Phoenix, Arizona 85045)	
CRD# 2233684)	
)	
Respondents.)	

14 RESPONDENT INTERSECURITIES, INC. ("ISI" or "RESPONDENT") elects to
15 permanently waive its right to a hearing and appeal under Articles 11 and 12 of the Securities Act
16 of Arizona, A.R.S. § 44-1801, et seq. ("Securities Act") with respect to this Order and Consent to
17 Same by: Respondent InterSecurities, Inc. ("Order"). ISI admits the jurisdiction of the Arizona
18 Corporation Commission ("Commission"); neither admits nor denies the Findings of Fact and
19 Conclusions of Law contained in this Order; and consents to the entry of this Order by the
20 Commission. The Findings and Conclusions made in this Order are entered for the purposes of
21 this proceeding only and not for any other purposes.

22 **I.**

23 **FINDINGS OF FACT**

24 1. ISI is a securities dealer whose business address is 570 Carillon Parkway, St.
25 Petersburg, Florida, 33716-1202.
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1 2. At all relevant times, ISI has been registered as a securities dealer in Arizona.

2 3. Gregory Brown ("Brown"), (CRD No. 2233684), whose last known address is
3 16417 South 15th Drive, Phoenix, Arizona 85045, was registered as a securities salesman with ISI
4 from August 1995 until October 2001. Brown operated as an independent businessman through his
5 company Financial Benefits Group, Inc.

6 4. Beginning in or around April 1999 through about August 2000, Brown offered and
7 sold investments involving payphones sold together with service or lease-back agreements. These
8 investments were securities in the form of investment contracts. The issuers of these investments,
9 including companies known as Phoenix Telecom, LLC ("Phoenix"), ETS Payphones, Inc. ("ETS"),
10 and Alpha Telcom ("Alpha"), marketed the investments as "business opportunities".
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12 5. The Phoenix and ETS payphone investments included the sale of payphones
13 together with lease-back agreements. Investors would share in the profits generated by operation of
14 their pay telephones. Investors would enter into two agreements, a purchase agreement, and a
15 lease-back agreement with Phoenix or ETS to manage the phone. The two agreements were
16 presented and promoted simultaneously. The telephones were presented to potential investors with
17 three options in the way of service contracts, each varying in the amount of service provided. The
18 three options varied from Option 1, which included a minimum of service, to Option 3, which
19 provided full service to the purchaser, including choosing a site and installing the telephone,
20 collecting all revenue from the telephone's operation, repairing the telephone when necessary, and
21 repurchasing or buying back the telephone at the investor's option. In the Phoenix and ETS
22 investments, the price of each phone was \$7,000 under the full-service option; the distribution was
23 \$82.25 per month for each phone. Although the written contracts offered investors a choice of
24 using a company other than ETS to manage the phone, no Arizona investor to whom Brown sold
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1 the investment picked a company other than ETS to manage their phones. A "typical return" on
2 each pay telephone was touted as 14% per year.

3 6. Alpha and its affiliates sold pay telephones with telephone service agreements
4 pursuant to which the investor would share in the profits of the pay telephone. Investors would
5 enter into two agreements, a purchase agreement, and a service agreement with Alpha to manage
6 the phone. The two agreements were presented and promoted simultaneously. The telephones were
7 presented to potential investors with four options in the way of service contracts, each varying in
8 the amount of service provided. The four options varied from Level 1, which included a minimum
9 of service, to Level 4, which provided full service to the purchaser, including choosing a site and
10 installing the telephone, collecting all revenue from the telephone's operation, repairing the
11 telephone when necessary, and even repurchasing or buying back the telephone at the investor's
12 option. Under Level 4, Alpha would split the net proceeds with the investor on a 70/30 basis, with
13 Alpha retaining 70% and the investor receiving 30%. The price of the pay telephones was the same
14 regardless of the service option chosen, \$5,000.00 per telephone. Although the written contracts
15 offered investors a choice of using a company other than Alpha to manage the phone, no Arizona
16 investor to whom Brown sold the investment picked a company other than Alpha to manage their
17 phones. A "typical return" on each pay telephone was touted as 14% per year. In practice, all
18 purchasers received \$58.34 per month per pay telephone purchased, which amounted to exactly
19 14% per annum.
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22 7. In or around early 2000, Phoenix transferred all of its lease agreements with
23 investors to ETS. On September 11, 2000, ETS filed for bankruptcy protection in Delaware under
24 chapter 11 of the Bankruptcy Code, and investors stopped receiving their monthly payments.

25 8. In August 2001, Alpha filed for bankruptcy protection in Florida under chapter 11
26 of the Bankruptcy Code. Prior to this filing, Alpha's monthly payments to investors ceased.

1 9. Between September 1998 and August 2000, eight states issued orders against ETS,
2 Phoenix, or Alpha finding that the payphone investments involved the offer and sale of
3 unregistered securities. The law on this issue, however, was not clear during this time. In May
4 1997, the Sixth Circuit Court of Appeal held that a similar telephone investment with a leaseback
5 option was not a security. The Securities Division in Massachusetts found that ETS was not a
6 security in July of 2000. Further, the Eleventh Circuit Court of Appeal also held that ETS was not
7 a security. It was not until the United States Supreme Court issued its decision on January 13,
8 2004 that the law on this issue became more certain.

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10 **FAILURE TO SUPERVISE BY ISI**

11 10. In April 1999, pursuant to ISI's compliance procedures, Brown submitted a written
12 request to ISI's Compliance Department for approval to sell ETS and Phoenix pay telephones as an
13 outside business activity unrelated to ISI. Brown presented the Assistant Vice President of ISI's
14 Compliance Department, an experienced Compliance Officer, with due diligence he had conducted
15 on the companies and answered questions that the Compliance Officer had regarding the products.
16 The Compliance Officer asked Brown to contact the Securities Division ("Division") to make
17 inquiries concerning the status and legality of the payphone companies and products. In April
18 1999, based upon the information Brown reported to him regarding Brown's contact with the
19 Division and his review of materials regarding these products, the Compliance Officer made the
20 determination that Brown could conduct the sales of the pay telephones as an independent outside
21 business activity not involving ISI. Thereafter, Brown sold the telephones as an outside business
22 activity. ISI did not receive any remuneration from these sales, nor did ISI communicate with
23 Brown's customers regarding these products.
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1 11. An outside business activity is a business activity of a representative which is
2 conducted personally by that representative and does not include the broker-dealer with whom he is
3 registered.

4 12. In March 1996, ISI had denied a request made by another registered salesman in
5 Arizona for approval of outside business activity to sell payphones on behalf of another company,
6 AmTel Communications, Inc. ("AmTel"), based upon the determination that the payphones may be
7 considered securities. At the time this determination was made, the Securities and Exchange
8 Commission had already filed an action against AmTel. While AmTel sold payphones as did
9 Phoenix, ETS and Alpha, the products offered were similar but not identical to those subsequently
10 approved by the Compliance Officer.

11 13. In November 1999, ISI gave Brown written approval to sell Phoenix payphone
12 contracts as outside business activity not involving the sale of securities.

13 14. In March 2000, as part of regular compliance oversight activity, ISI approved the
14 request of another registered salesman in another state to engage in an outside business activity
15 involving Phoenix payphones. ISI limited this representative's activities with that company and
16 did not allow him to solicit investors.

17 15. In or around April 2000, Brown reported his activity involving the sale of Alpha
18 payphones to ISI in his Annual Regulatory Questionnaire for Calendar Year 1999. ISI did not
19 enforce its compliance procedures requiring a written request, or further review Brown's sale of
20 Alpha payphone contracts.

21 16. On or about July 14, 2000, Brown reported to ISI that his sale of these "phone
22 deals" generated approximately 50% of his compensation, with year-to-date compensation to
23 Brown of approximately \$200,000 for these sales.

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1 relying on that contact without further independent review was insufficient to satisfy ISI's
2 supervisory obligations.

3 6. ISI's conduct is grounds for administrative remedies and undertakings under A.R.S. §
4 44-1961(B).

5 **III.**

6 **ORDER**

7 THEREFORE, on the basis of the Findings of Fact, Conclusions of Law, and
8 RESPONDENT'S Consent to Entry of Order that is attached hereto and is a part hereof, the
9 Commission finds that the following relief is appropriate, in the public interest, and necessary for
10 the protection of investors:

11 IT IS ORDERED that RESPONDENT shall adopt and implement a claims procedure to
12 evaluate and resolve all remaining claims of investors who purchased payphone contracts from
13 Brown. This procedure shall include but is not limited to the following:

14 (1) Within 15 days of the effective date of this Order, ISI will prepare a letter, approved
15 by the Division, to be sent to all payphone customers of Brown, by certified mail
16 with return receipt requested, with a copy of this Order, informing them of their
17 options under the claims procedure. This claims procedure is expressly limited to
18 those individuals who purchased pay telephones through Brown. However, ISI will
19 not be responsible for claims submitted by Brown or relatives of Brown for their
20 own investments. Further, individuals who have already entered into settlements
21 with ISI are precluded from seeking any further recovery.

22 (2) Within 10 days of this Order, ISI will provide the names of proposed independent
23 arbiters to the Division. Upon mutual agreement with the Division, an arbiter will
24 be selected and retained by ISI within 30 days of this Order. The independent
25 arbiter shall have experience with the retail securities business and its governing
26 rules and regulations. Upon retention, the independent arbiter shall sign an oath to

1 fairly and justly determine the claims submitted to him or her pursuant to the
2 principles of law and equity applicable in the state of Arizona. The rules of
3 evidence should not be strictly applied except in cases of privilege.

4 (3) Claimants will have 60 days after receipt of ISI's letter referenced in (1) above to
5 present their claims to ISI; if the investor fails to do so, this process shall no longer
6 be available to the investor or any representative thereof. In no respect shall this
7 Order extend any applicable statutes of limitations or any other applicable defense
8 for investors who elect not to participate in this claims process. However,
9 otherwise applicable statutes of limitations shall not bar claims raised before the
10 independent arbiter pursuant to the provisions of this Order. This provision shall
11 not bar the applicability of the statute of limitations in any context other than this
12 claims process before the independent arbiter.

13 (4) Within 30 days of receipt of a claim, ISI will review the claim and make an offer to
14 settle the claim or reject the claim.

15 (5) The claimant can accept the offer or make a counter-offer within 30 days.

16 (6) If ISI and a claimant do not reach an agreement within 30 days of any offer or
17 counter-offer, ISI will forward the claim to the independent arbiter. Within 15
18 business days of the submission of the claim, ISI may serve a written response to
19 the claim. The claimant shall have 15 business days from the date of service of the
20 response to submit a reply, if so desired. Thereafter, the independent arbiter may
21 decide the claim on the papers submitted or, if he deems necessary, may interview
22 the claimant or request further written information from either of the parties. ISI
23 and the claimant shall each be entitled to have a representative present, either in
24 person or by phone, at any claimant interview. It is anticipated that in most
25 circumstances the independent arbiter will make his determination based upon the
26 parties' written submissions. The independent arbiter may engage in additional

1 information gathering as deemed necessary, including without limitation requests
2 for documents or information from any party to this administrative action or any
3 claimant in this claims procedure. The independent arbiter will issue his
4 determination within 60 days of receipt of the claimant's reply or from the date
5 such reply was due if the claimant chose not to submit a reply. All submissions
6 made to the independent arbiter by either party shall be served on the other party on
7 the same date and in the same manner and means as it was served on the arbiter.
8 Service may be effected by mail or other means of delivery and is accomplished on
9 the date of mailing, if by U.S first-class postage or by means of overnight delivery,
10 or on the date of transmission if by facsimile.

11 (7) The decision of the independent arbiter shall be final and binding, and not subject to
12 challenge or appeal, except in the case of fraud or misconduct on the part of the
13 independent arbiter.

14 (8) Any investor who elects the claims process under the Order shall be required, upon
15 such election, to execute a consent by which they agree to be bound by the
16 determination of the independent arbiter and specifically waive and release any
17 other remedies they may have (and fully release ISI, and any representatives
18 currently or formerly associated with ISI, and any current or former officers,
19 directors, principal employees, attorneys, agents or affiliates of ISI), including the
20 right to arbitrate in any forum or to bring a claim in court or before any
21 administrative or arbitral body, either individually or as a member of any class in
22 connection with this investment through Brown. If any investor has already
23 initiated arbitration against ISI, his or her consent shall include that the
24 determination of the independent arbiter will resolve all claims brought by them
25 including those brought in arbitration and upon receipt of payment from ISI, the
26 investor will dismiss any pending proceeding with prejudice. This Order does not

1 create or revive any rights against ISI which have heretofore been released or
2 extinguished.

3 (9) The arbiter's decision on each investment shall not exceed the investor's purchase
4 price less the amount of any distributions received on the investment ("actual net
5 out-of-pocket loss"). The independent arbiter shall not be permitted to award
6 punitive damages or attorneys' fees. Any amount awarded shall not exceed the
7 actual net out-of-pocket loss sustained by the investor.

8 (10) ISI will remit payment to the claimant within 20 days of receipt of the independent
9 arbiter's determination of each claim.

10 (11) Neither ISI nor the Division will encourage or discourage, either directly or
11 indirectly, any investor from participating in the claims process or from selecting
12 any particular alternative for evaluation of his or her claim. This language shall not
13 prohibit ISI from resolving any claim independent of this claims process. In the
14 event ISI receives a release regarding any payphone purchase, such purchaser shall
15 no longer be eligible for submission in this claims process.

16 (12) ISI will pay the reasonable cost of the independent arbiter and indemnify the arbiter
17 against all claims related to his or her work as the independent arbiter. The
18 independent arbiter will be paid based on a predetermined hourly rate and shall
19 provide ISI with monthly statements of his or her fees and incidental expenses.

20 (13) The independent arbiter shall not enter into any employment, consulting or
21 attorney-client relationship with ISI, or any of its present or former parents,
22 subsidiaries, directors, officers, employees or agents acting in their capacity for the
23 period of engagement and for a period of one (1) year from the completion of his or
24 her engagement, nor shall she/he or her/his firm appear in any civil proceeding
25 adverse to ISI on behalf of any customer or former customer of ISI.
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1 IT IS FURTHER ORDERED that RESPONDENT, each month after entry of this Order,
2 until all claims are fully processed pursuant to this Order, shall provide the Division a detailed
3 status report and accounting of all claims, offers, resolutions, and unresolved claims.

4 IT IS FURTHER ORDERED that ISI's Consent to Entry of Order that is attached hereto is
5 incorporated herein by this reference and made a part of this Order, including specifically, but not
6 limited to, paragraphs 6 and 7 thereof.

7 IT IS FURTHER ORDERED that ISI's entry into this Order and Consent and
8 implementation of practices and procedures regarding outside business activities shall resolve all
9 ongoing investigations and inquiries relating to ISI. Should new customer complaints be filed with
10 the Division after entry of the Order unrelated to the matters currently under consideration by the
11 Division, nothing herein shall be construed as prohibiting the Division from initiating a new
12 investigation or examination of any such complaint.

13 IT IS FURTHER ORDERED that RESPONDENT shall adopt and implement remedial
14 measures and new supervisory and compliance procedures in accordance with a plan submitted to
15 the Division. These procedures include, but are not limited to:

- 16 a) Within 30 days of entry of this Order, implement written compliance procedures
17 with respect to the review of outside business activities designed to ensure that such
18 activities do not involve the sale of unregistered securities.
- 19 b) Within 30 days of entry of this Order, implement specific written procedures which
20 require Compliance and/or Legal Department to document their review of whether
21 a requested outside business activity involves the sale of unregistered securities.
22 Such procedures shall include but not be limited to requiring that all contacts with
23 the Arizona Securities Division be handled directly by the Compliance or Legal
24 Department, and not delegated to individual salesmen or any other person without
25 compliance and/or legal training and decision-making responsibility.
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1 IT IS FURTHER ORDERED that RESPONDENT, within 180 days of the entry of this
2 Order, shall conduct an on-site inspection and audit of each registered representative working from
3 a location in Arizona. These audits will be documented and provided to the Division within 30
4 days of the completion of each audit. Thereafter, audits will be performed in Arizona at least semi-
5 annually for a period of two years from the entry of this Order. The audits will include, but not be
6 limited to, specific review of the following:

- 7 • private securities activity and outside business activity by registered securities salesmen
8 not approved by ISI; and
- 9 • approved outside business activity involving the offer or sale of products that may
10 constitute unregistered securities.

11 IT IS FURTHER ORDERED, pursuant to A.R.S. § 44-1961(B), that RESPONDENT shall
12 pay administrative penalties in the amount of \$50,000 payable to the "State of Arizona." Payment

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shall be made by company check to the State of Arizona due and payable on the date of this Order, without notice or demand.

IT IS FURTHER ORDERED that this Order shall become effective immediately upon the date set forth below.

BY ORDER OF THE ARIZONA CORPORATION COMMISSION

<u>/s/ Marc Spitzer</u>	<u>William A. Mundell</u>	<u>Jeffrey Hatch-Miller</u>
CHAIRMAN	COMMISSIONER	COMMISSIONER

<u>Lowell Gleason</u>	<u>Kristin Mayes</u>
COMMISSIONER	COMMISSIONER

IN WITNESS WHEREOF, I, BRIAN C. McNEIL, Interim Executive Secretary of the Arizona Corporation Commission, have hereunto set my hand and caused the official seal of the Commission to be affixed at the Capitol, in the City of Phoenix, this 20th day of October, 2004.

/s/ Brian C. McNeil
BRIAN C. McNEIL
Executive Secretary

DISSENT

This document is available in alternative formats by contacting Yvonne L. McFarlin, Executive Assistant to the Executive Secretary, voice phone number 602-542-3931, E-mail ymcfarlin@cc.state.az.us.

(PTJ)

CONSENT TO ENTRY OF ORDER

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2 1. RESPONDENT INTERSECURITIES, INC. ("ISI") admits the jurisdiction of the
3 Commission over the subject matter of this proceeding. ISI acknowledges that it has been fully
4 advised of its right to a hearing to present evidence and call witnesses and ISI knowingly and
5 voluntarily waives any and all rights to a hearing before the Commission and all other rights
6 otherwise available under Article 11 of the Securities Act and Title 14 of the Arizona
7 Administrative Code. ISI acknowledges that this Order and Consent to Same by: InterSecurities,
8 Inc. ("Order") constitutes a valid final order of the Commission.

9 2. ISI knowingly and voluntarily waives any right it may have under Article 12 of the
10 Securities Act to judicial review by any court by way of suit, appeal, or extraordinary relief
11 resulting from the entry of this Order.

12 3. ISI acknowledges and agrees that this Order is entered into freely and voluntarily
13 and that no promise was made or coercion used to induce such entry.

14 4. ISI acknowledges that it has been represented by counsel in this matter, it has
15 reviewed this Order with its attorney and understands all terms it contains.

16 5. ISI neither admits nor denies the Findings of Fact and Conclusions of Law
17 contained in this Order. ISI consents to the entry of the Findings of Fact and Conclusions of Law
18 for purposes of this proceeding only and not for any other purposes.

19 6. The Division and ISI desire to establish an appropriate mechanism to expeditiously
20 and equitably address any financial loss suffered by individuals who purchased pay telephones
21 through Brown. For any person or entity not a party to this Order, this Order does not limit or
22 create any private rights or remedies against ISI or limit or create liability of ISI, or limit defenses
23 of ISI to any claims. However, nothing in this Order shall limit the Division from using this Order
24 in any proceeding against ISI in the future should one arise.

25 7. By consenting to the entry of this Order, ISI agrees not to take any action or to
26 make, or permit to be made, any public statement denying, directly or indirectly, any Finding of

1 Fact or Conclusion of Law in this Order or creating the impression that this Order is without
2 factual basis. ISI will undertake steps reasonable to assure that all of its agents and employees
3 understand and comply with this agreement. Except as related to the statute of limitations in
4 paragraph (3) at page 8 of this Order, nothing in this Order and ISI's Consent to Entry of Order,
5 including the Findings and Conclusions contained therein, shall in any way limit ISI's ability to
6 defend itself and/or take any contrary position of fact or law in any subsequent litigation or other
7 proceeding, including claims determinations pursuant to this Order, in which the Commission is
8 not a party.

9 8. While this Order settles all administrative matters between ISI and the Commission,
10 ISI understands that this Order does not preclude the Commission from instituting future
11 administrative proceedings based on violations or information of which the Commission is not
12 aware and that are not addressed by this Order.

13 9. ISI understands that this Order does not preclude the Commission from referring
14 this matter to any governmental agency for administrative, civil, or criminal proceedings that may
15 be related to the matters addressed by this Order.

16 10. ISI understands that this Order does not preclude any other agency or officer of the
17 state of Arizona or its subdivisions from instituting administrative, civil or criminal proceedings
18 that may be related to matters addressed by this Order.

19 11. ISI consents to the entry of this Order and agrees to be fully bound by its terms and
20 conditions. If ISI breaches any provision of this Order, the Commission may vacate this Order and
21 restore this case to its active docket.

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12. Tom Moriarty represents that he is President of INTERSECURITIES, INC. and has been authorized by INTERSECURITIES, INC. to enter into this Consent to Entry of Order for and on behalf of INTERSECURITIES, INC.

INTERSECURITIES, INC.
a Delaware Corporation

BY: /s/ Thomas R. Moriarty

TITLE: President

SUBSCRIBED AND SWORN TO BEFORE me this 22nd day of September, 2004.

/s/ Diana J. Garrand
NOTARY PUBLIC

My Commission Expires:
November 22, 2006

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